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Page

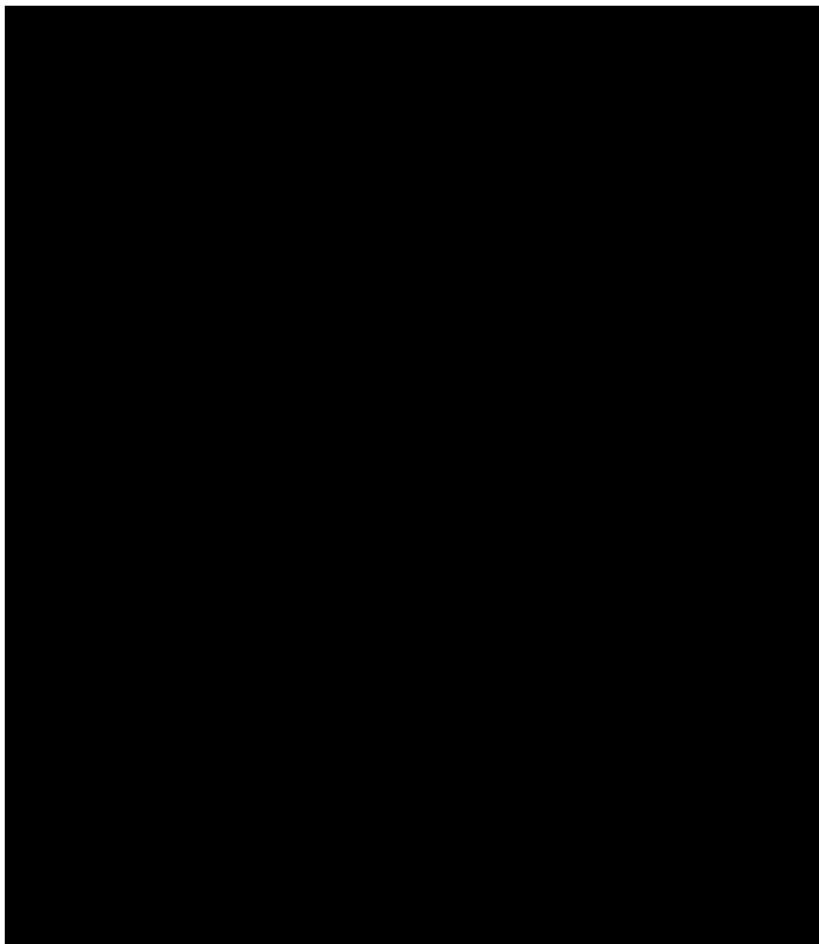


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The Indo-Nepalese Dispute: The View From the Terai [REDACTED]

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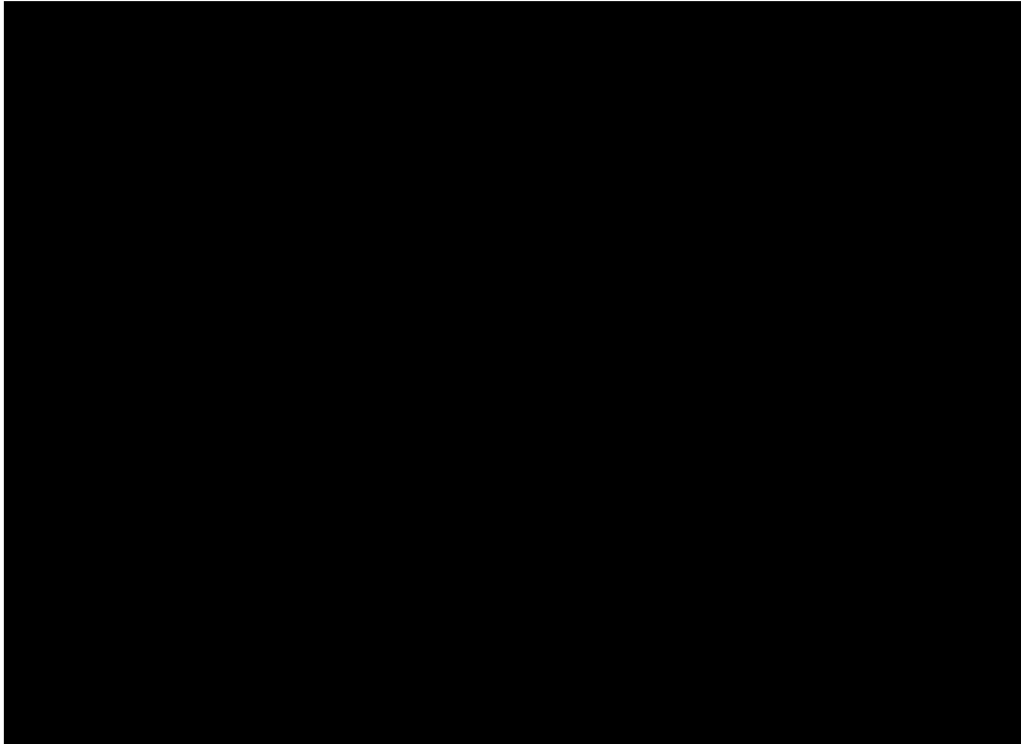
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The important Terai region of southern Nepal is experiencing severe economic problems because of the dispute between India and Nepal that has prevented the renewal of a trade and transit agreement. Despite the hardships, the dispute has not sparked political unrest in the region. [REDACTED]

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The Indo-Nepalese Dispute: The View From the Terai

Much of the publicity surrounding Nepal's continuing dispute with India centers on the diplomatic maneuvering between Kathmandu and New Delhi, but Nepalese outside the capital are bearing the brunt of the economic hardships caused by the impasse. The Terai—the southern belt of Nepal that borders India—has been particularly hard hit by fuel shortages, inflation, and the loss of the Indian export market.

Despite the hardships, the dispute has not sparked political unrest in the Terai, probably because the opposition is factionalized and many residents view New Delhi, not Kathmandu, as the culprit. Kathmandu recognizes that political dissent is a potential problem and is trying to inject funds into the region to prevent dissaffection from developing. The economic problems in the Terai growing out of the dispute probably have helped convince Kathmandu that it has few options aside from dependence on India.

Nepalese leaders are concerned about the Terai because of its strategic location adjacent to India and its large contribution to Nepal's economy. Indian laborers hold many of the skilled and semiskilled jobs there, raising concerns in Kathmandu about potential unrest in the area sponsored by New Delhi. Nepal's industrial base is in the Terai, which also is the source of almost 60 percent of the country's agricultural production.

New Delhi Squeezes Import-Export Markets

India reacted to the expiration of the trade and transit agreements in March by tightening an economic noose around Nepal. New Delhi closed 13

1 The dispute nominally centers on a trade and transit agreement that expired in March. The disagreement, however, covers several broader issues, including India's concerns about Kathmandu's treatment of Indian laborers in Nepal; New Delhi's worries about Nepal's ties to China; and King Birendra's desire to assert Nepal's sovereignty and alter the traditionally close Indo-Nepalese relationship. Some of these issues are outlined in a 1950 treaty of peace and friendship, but the two sides do not agree on how that treaty should be interpreted and each claims the other has violated it.

of 15 crossing points along the 800-kilometer border and raised duties for Nepalese goods. India also cut off the supply of critical commodities, such as petroleum products and coal, that it had provided to Nepal under separate commercial agreements.

India's moves had a quick and clear impact on Nepal's economy, particularly in industrial towns in the Terai. Some industries in border towns that had exported their production to India before the dispute are closing or scrambling for new buyers. Energy problems are particularly acute. Nepal's coal imports now cost more than before the trade impasse.

Economic Issues Dominate in the Terai

India's reaction to the dispute has kept most residents of the Terai occupied more with economic problems than with opposition to the government's handling of the impasse. Shopkeepers say that costs have risen about 25 percent. Many goods are available but at sharply higher prices. The economic problems growing out of the dispute also are slowing development projects in the region.

Industrial shutdowns and slowdowns are common in the region. Three of four jute mills in the border town of Biratnagar have shut down since the dispute erupted in March, and other operations—such as textile mills—have closed elsewhere. A new Indian duty of 140 percent has made Nepalese jute uncompetitive across the border, where Nepalese firms exported about 60 percent of their jute before the dispute. Several factors growing out of the dispute explain the industrial problems: high transport costs, fuel shortages, and the duties that are closing the Indian market.

The economic slowdown is affecting the national economy. The International Monetary Fund, for example, estimates that Nepal's growth will drop from 5.3 percent to -2.2 percent during the current fiscal year. Part of this drop stems from the economic

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stagnation in the Terai. Nepal's economic problems have led for the first time to speculation in Indian rupees in the Terai. [REDACTED]

Most businesses and small merchants are turning to the black market for scarce commodities. Smuggling is open and acknowledged in the Terai. [REDACTED]

[REDACTED] even by managers of state-owned enterprises. Although the black market has helped keep some Nepalese businesses alive — such as cigarette factories that are buying tobacco smuggled from India — the surcharges levied by smugglers are fueling inflation in the Terai. [REDACTED]

Opposition Failing To Capitalize on Difficulties

The economic problems have not sparked significant political unrest in the Terai. The dispute with India has not markedly raised political activity in the normally placid region, and businessmen and merchants [REDACTED] appear mainly concerned with the impact on their pocketbooks. Press [REDACTED] reporting indicates that students, often the most active group in Nepal, are relatively dormant in the Terai and that labor groups have maintained their traditional aloofness from antigovernment agitation. [REDACTED]

We believe the political scene in the Terai is largely quiet in part because the factionalized opposition is not strong enough to organize protests. Neither the Nepalese Congress Party nor any of the many factions of the Communist Party of Nepal has had much success in stirring up antigovernment agitation, and factionalism almost certainly has contributed to their failure. In addition, Nepalese law proscribes political parties, and the government frequently nips antigovernment agitation in the bud by arresting political leaders. Police arrested leaders of the Congress Party and Communist groups following demonstrations in the Terai in mid-December, according to press reports. [REDACTED]

The limited political reaction also stems from the nationalism of the Terai's residents, who feel more affinity for Kathmandu's position than for India's. [REDACTED] Nationalist sentiment apparently has made some Terai residents — fearful of being seen as pro-Indian — hesitant to criticize Kathmandu's failure to resolve the dispute, despite the economic problems. [REDACTED]

The Terai

The Terai forms Nepal's southern tier, which accounts for about 20 percent of the country's land and more than 40 percent of its population of 17.6 million. A flat, dry region, the Terai falls outside what many Nepalese consider Nepal proper: the central hill tier that is the historical site of princely states and kingdoms and now includes the modern capital of Kathmandu. [REDACTED]

Nepalese migration to the Terai began in earnest during the 1950s, when foreign aid helped eradicate a virulent strain of malaria that had inhibited population growth. Indian and Nepalese landlords used Indian labor to work the Terai before the area was cleared of malaria, and the Indian background of most Terai residents has resulted in discriminatory citizenship policies and questions about their political loyalties. Many Nepalese in the Kathmandu Valley and the central hill regions of the country regard the people of the Terai with suspicion because of the historically close relationship between India and the Terai. [REDACTED]

[REDACTED] the Terai is reaching its saturation point. Farmers are cultivating much of the lowland area, and soil fertility is declining. Nepal's population distribution has changed steadily since the 1950s as farmers who exhausted the arable land in the hills moved south. The Terai now has the country's highest population density, and migration to the region from both India and the hill regions of Nepal will probably increase. [REDACTED]

The dispute has exposed tensions between the lowland Terai dwellers and the residents of the hill region, which is regarded as the heartland of Nepal.

The Government's View

We believe the government is focusing on several economic tactics to keep the Terai quiet. According to Embassy reports, laborers laid off from mills in the

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region are receiving half-salaries from the government. Kathmandu also is pressing mill operators to remain open. [REDACTED]

Despite the low level of political dissent, government officials are concerned that India will try to fan discontent in the Terai. [REDACTED]

probably will remain quiet for the near term. The economic problems in the Terai caused by the dispute almost certainly have convinced Kathmandu that Nepal's economic future lies in its ties to India. The government had hoped to find alternatives to India when the dispute began, but India's favorable import/export terms and geographic proximity to Nepal have proven impossible to replace. Although some businesses in the Terai are looking to China as a potential export market, poor transport links make a major increase in Sino-Nepalese trade unlikely.

[REDACTED]

[REDACTED]

Outlook

We believe Nepal's opposition parties will be unable to use the dispute to spark unrest, and the region

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